INTERSTATE DEPARTMENT STORES, INC.

(A DELAWARE CORPORATION)

NEW YORK, N. Y.

ANNUAL REPORT

YEAR ENDED

JANUARY 31, 1947

INTERSTATE DEPARTMENT STORES, INC.

DIRECTORS

Robert S. Adler
Russell P. Bygel
Reagan P. Connally
Charles E. Federman
Paolino Gerli
R. C. Kramer
Will I Levy
Harold F. Linder
Frank J. Meley
Albert Parker
Harold J. Szold

OFFICERS

President	Reagan P. Connally
Chairman of the Board	R. C. Kramer
Executive Vice President	Russell P. Bygel
Vice President and Treasurer	Frank J. Meley
Secretary	Albert Parker
Assistant Treasurer	M. Grant Berens
Assistant Secretary	Edward C. Schenkel

Transfer Agent	Bank of the Manhattan Company	New York
Registrar	The Commercial National Bank and Trust Company	New York
General Counsel	Parker, Chapin and Flattau	New York
Public Accountants	S. D. Leidesdorf & Co.	New York
Executive and General Offices	111 Eighth Avenue	New York

April 15, 1947

To the Stockholders of
INTERSTATE DEPARTMENT STORES, INC.

Submitted herewith is the Annual Report and Financial Statements of Interstate Department Stores, Inc. and its subsidiaries for the fiscal year ended January 31, 1947.

The comparative operating results of the Company may be briefly summarized as follows:

	1946	1945
Total Sales	$52,320,000	$44,328,000
Profit before Federal Income Taxes	2,460,000	2,973,000
Profit after Federal Income Taxes	1,410,000	1,056,000
Earned per Share	4.56	3.42
Dividends Paid per Share	1.70	1.40

SALES: Total sales increased 18%, leased department sales increased 9% and owned department sales increased 19% in 1946 over 1945. Your Company has a larger proportion of its business in lower price lines of merchandise than the typical retailer. Good merchandise in such categories was not available in as large quantities as in higher price lines. The effect of merchandise shortages on the Company's sales was greater than on retailing generally. It is anticipated that adequate supplies of most types of goods that we sell will be available in 1947 in price lines suitable for our customers.

PROFITS: Although sales volume increased, profits before Federal taxes decreased $513,000. This decrease was caused by reduced gross margin and by increased expense. The gross margin of your Company in 1946 was 1.8% below 1945, and was in fact the lowest since 1938. This low gross margin was caused by government price regulation during most of the year and by the policy of management of selling quickly existing stocks as better quality merchandise became available. Heavy markdowns were taken in 1946 to force sales of merchandise which was below the standards of quality and value currently being produced.

Increased expenses resulted in part from increased dollar volume, increase in salary and wage costs and increase in cost of supplies and services.

NET PROFITS: The increase in net earnings was caused entirely by the reduction in Federal income taxes resulting from the elimination of the excess profits tax.

DIVIDENDS: Your directors believe dividends should be the largest that can safely be paid consistent with the operating requirements of your Company. In October 1946 the quarterly dividend rate was increased to 50¢ per share from the 35¢ quarterly dividend rate established in April 1945. $1.70 per share was paid in dividends in 1946 compared with $1.40 in 1945. Later in this report is a brief summary of the working capital requirements of your Company which will be a major factor in determining future dividend policy.

INVENTORIES: Inventories were $3,300,000 higher at January 31, 1947 than they were a year previous. This increase in inventory was caused in part by higher prices. Prior to the war your Company had a relatively small "hard lines" business, i.e., sale of furniture, major electrical appliances, home furnishings, etc. A substantial volume was developed from them in 1946 and plans have been made for a further expansion of these lines in 1947. Part of the increase in total inventory is caused by the inventory required for those stores that have already started "hard lines" sales.

In some categories of merchandise, inventories are higher than management would prefer. Control of inventories, elimination of undesirable goods from inventory as more desirable merchandise is manufactured and scrutiny of inventory valuations has and will continue to be one of the most important management problems.

Analysis of the age of the inventory shows that 98.7% is less than one year old and 1.3% over one year old. A year ago 98.4% was under one year and 1.6% over one year. Although this merchandise was taken

in inventory at reduced prices, in addition, reserves have been established to provide for such losses as may be experienced in the sale of this merchandise.

COMMITMENTS: Future orders for merchandise on January 31, 1947 were approximately $3,900,000, a reduction of $2,500,000 or 39% from the previous year. The total of inventories and outstanding orders January 31, 1947 was $12,900,000, an increase of 3% over the previous year. The owned department sales increase for the past year was 19%. In general, therefore, the increase in inventory and orders was comparable to the increase in sales.

WORKING CAPITAL: Net working capital increased $294,000 during the year after payment of $400,000 on the Company's term bank loan and amounted to $8,665,000 at year end. This is the largest working capital in the history of the Company. Despite this increase, however, the Company has substantial additional working capital requirements. Six new small stores were opened in 1946 and additional new stores will be opened in 1947. Modernization of, and deferred repair and maintenance work in, existing stores will require substantial sums. There will be substantial cash requirements to finance increased inventories for "hard lines" and to finance the growing volume of installment business that will flow from increased sales of "hard lines." In addition, the agreement of the Company with its banks provides for annual payments of $200,000 on its long term loan. It is obvious therefore that the Company must follow a cautious policy in disbursing its earnings in cash dividends.

NEW STORES OPENED AND STORES CLOSED: New stores were opened in 1946 in Edgerton, Wisconsin; Muncy, Pennsylvania; Whitinsville, Massachusetts; Front Royal, Virginia; Canaan, Connecticut, and a small neighborhood store in Philadelphia. Additional stores will be opened in 1947. The Trenton store was closed in 1946. This store had been unprofitable under the real estate lease which expired in 1946 and when that lease could only be renewed under still higher rent, it was decided to close the store.

MODERNIZATION—MAJOR DEFERRED MAINTENANCE AND REPAIRS: $640,000 was spent in 1946 for modernization of stores: $215,000 of this sum was charged to current operations and $425,000 was added to fixed assets. The inability to perform major building and maintenance work during the war has caused a large amount of this work to accumulate. Government building restrictions and high prices for construction work have delayed the progress management had hoped to make on this problem. Substantial sums will have to be spent for these purposes in the next several vears in order to insure that the local competitive position of your stores is continually improved.

RETIREMENT PLAN: $130,000 was contributed to the Company's Retirement Income Plan for 1946 under the authorization previously given to the Company by the stockholders.

ORGANIZATION: The organization of the Company was strengthened during the year by the return of many key employees of the Company from war service. District Managers were appointed to supervise groups of stores in contiguous geographical areas. We expect improved results from the present form of the operating organization. 1946 was a difficult year in many respects for your Company and the management wishes to take this opportunity to thank the several thousand employees of the Company for their splendid efforts during that year.

OUTLOOK: Your Company enters 1947 with a strengthened organization. It expects a greater supply of sound valued quality merchandise for customers of moderate income in 1947 than was available in 1946. It should develop a large volume of "hard line" business. Retail volume is dependent to a large degree on the income level of the nation. We believe that the share of such volume that your Company will secure in 1947 will not be less than it received in 1946.

Yours very truly,

Reagan P. Connally,
President

INTERSTATE DEPAR

AND SUBSIDIAR

CONSOLIDATED BALANCE SH

ASSETS

	As at January 31, 1947		As at January 31, 1946	
CURRENT ASSETS:				
Cash on hand and in banks		$ 1,027,676		$ 4,434,683
U. S. Treasury Savings Notes—Series C (at cost) and accrued interest		90,291		530,221
Accounts Receivable:				
Customers	$1,772,045		$973,612	
Less: Reserves	212,955	1,559,090	174,208	799,404
Other	400,469		250,566	
Less: Reserve	3,883	396,586	4,399	246,167
Merchandise inventories—(Note A)		8,735,191		5,427,523
Total Current Assets		11,808,834		11,437,998
OTHER ASSETS:				
Miscellaneous other assets, less reserves		161,635		106,252
FIXED ASSETS—AT COST:				
Land	103,210		50,624	
Buildings	55,890		115,985	
Less: Reserve for depreciation	3,996		1,202	
	51,894		114,783	
Alterations and improvements to leased premises	218,514		447,366	
Less: Reserve for depreciation	44,362		341,438	
	174,152		105,928	
Furniture and equipment	1,528,920		1,329,393	
Less: Reserve for depreciation	619,932		635,249	
	908,988	1,238,244	694,144	965,479
LEASEHOLDS	196,529		288,529	
Less: Reserve for amortization	122,315	74,214	199,120	89,409
DEFERRED CHARGES		489,897		411,868
		$13,772,824		$13,011,006

The Notes to Financial Statements are an integral part of t

TMENT STORES, INC.

RY COMPANIES

IEET AS AT JANUARY 31, 1947

LIABILITIES

	As at January 31, 1947		As at January 31, 1946	
Current Liabilities:				
Accounts payable—trade creditors (including liability for merchandise in transit)		$ 1,577,837		$ 1,644,783
Accrued salaries, interest and expenses		1,093,903		817,561
Accrued Federal taxes on income—(Note C)	$1,212,141		$2,061,167	
Less: U. S. Treasury Savings Notes—Series C (at cost) and accrued interest	1,212,141	—	2,061,167	—
Accrued taxes—other—(Note C)		324,954		279,993
Sundry other laibilities		96,841		124,241
Mortgage Payable—due within one year		50,000		—
Long term debt—due within one year (Note B)		—		200,000
Total Current Liabilities		3,143,535		3,066,578
Long Term Debt:				
Notes payable—banks, due August 27, 1955—(Note B)	2,100,000		2,500,000	
Less: Amount due within one year	—	2,100,000	200,000	2,300,000
Total Liabilities		5,243,535		5,366,578
Capital Stock and Surplus (Note B):				
Common Stock—Without Par Value:				
Authorized ... 320,000 Shares				
Issued and Outstanding ... 308,946 Shares	1,580,252		1,580,252	
Capital Surplus—per Consolidated Statement of Surplus	1,915,949		1,915,949	
Earned Surplus—per Consolidated Statement of Surplus	5,033,088	8,529,289	4,148,227	7,644,428
		$13,772,824		$13,011,006

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INTERSTATE DEPARTMENT STORES, INC.

AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF PROFIT AND LOSS FOR THE YEAR ENDED JANUARY 31, 1947

	For the Year Ended January 31, 1947		For the Year Ended January 31, 1946	
Net Sales:				
Own departments	$46,502,752		$38,995,710	
Leased departments	5,817,308	$52,320,060	5,331,954	$44,327,664
Cost of Sales, Operating and Administrative Expenses		49,679,784		40,999,575
		2,640,276		3,328,089
Less:				
Depreciation—buildings, alterations and improvements, fixtures and equipment	222,819		201,546	
Amortization—leaseholds	15,195	238,014	14,852	216,398
		2,402,262		3,111,691
Other Income—Net		120,924		92,258
		2,523,186		3,203,949
Less:				
Interest paid	63,117		100,429	
Premiums paid on retirement of long term debt	—	63,117	130,831	231,260
Net Profit, Before Provision for Federal Taxes on Income		2,460,069		2,972,689
Provision for Federal Income Taxes	1,050,000		545,000	
Provision for Federal Excess Profits Taxes	—	1,050,000	1,372,000	1,917,000
Net Profit—per Consolidated Statement of Surplus		$ 1,410,069		$ 1,055,689

CONSOLIDATED STATEMENT OF SURPLUS FOR THE YEAR ENDED JANUARY 31, 1947

	For the Year Ended January 31, 1947	For the Year Ended January 31, 1946
Earned Surplus (Note B):		
Balance—beginning of period	$4,148,227	$3,525,062
Add: Net profit for the year ended January 31, 1947-1946—per Consolidated Statement of Profit and Loss	1,410,069	1,055,689
	5,558,296	4,580,751
Deduct: Dividends paid on Common Stock	525,208	432,524
Balance—end of period—per Consolidated Balance Sheet	$5,033,088	$4,148,227
Capital Surplus (Note B):		
Balance—beginning of period	$1,915,949	$1,915,949
Balance—end of period—per Consolidated Balance Sheet	$1,915,949	$1,915,949

The Notes to Financial Statements are an integral part of these statements and should be read in conjunction herewith.

INTERSTATE DEPARTMENT STORES, INC.

AND SUBSIDIARY COMPANIES

NOTES TO FINANCIAL STATEMENTS
AS AT JANUARY 31, 1947

NOTE A—Merchandise inventories, as at January 31, 1947, which include merchandise in transit in the amount of $226,973, are stated on the following bases which are consistent with those used in the preceding year:

At Stores —At the lower of cost, or market, as calculated by the retail method of inventory valuation, after provision for markdowns based on age of merchandise.

At Warehouses—At the lower of cost (substantially on the "First in, First out," basis) or replacement market.

In Transit —At specific invoice cost.

NOTE B—The loan agreement with respect to the long term debt contains certain restrictions on the right of the Company to declare dividends (other than stock dividends). As at January 31, 1947 approximately $2,217,000 of the Company's surplus was not subject to such restrictions. The said amount will be increased or decreased primarily to the extent that future consolidated net income is in excess of or less than future dividend distributions.

The loan agreement further provides that on August 27 of each year payments of $200,000 are required to be made on the loan. The payment due August 27, 1947 was paid in advance during the current year with the result that no installment is due until August 27, 1948.

NOTE C—The financial statements are subject to final determination of Federal and state taxes. The Federal income and excess profits tax returns have been examined through the fiscal year ended January 31, 1944 and all additional assessments thereon have been paid.

ACCOUNTANTS' REPORT

TO THE BOARD OF DIRECTORS,
INTERSTATE DEPARTMENT STORES, INC.,
NEW YORK, N. Y.

We have examined the consolidated balance sheet of Interstate Department Stores, Inc. and subsidiary companies as at January 31, 1947 and the consolidated statements of profit and loss and surplus for the year then ended; have reviewed the system of internal control and the accounting procedures of the companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the companies and other supporting evidence by methods and to the extent we deemed appropriate. Our examination was made in accordance with generally accepted auditing standards applicable in the circumstances and included all procedures which we considered necessary.

Our examination of the merchandise inventories included a general review of the inventory procedures and records, including the retail inventory records, and tests to determine the mathematical accuracy of the inventory schedules. In addition, our representatives were present at the Company's principal warehouse as well as at certain stores, which we considered to be representative and which we selected for test purposes, to determine that the inventory procedures were carried out effectively and to make tests of the quantities in the inventory. We also communicated directly with vendors who are holding Company's merchandise pending delivery instructions from the Company. Our examination of the customers' accounts receivable included tests by direct communication with a selected number of customers at stores selected by us.

In our opinion, the accompanying consolidated balance sheet and related consolidated statements of profit and loss and surplus, together with the Notes to Financial Statements, present fairly the consolidated position of Interstate Department Stores, Inc. and subsidiary companies at January 31, 1947, and the consolidated results of their operations for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

S. D. LEIDESDORF & CO.

New York, N. Y.
March 31, 1947.

This report is solely for statistical information for stockholders, and is not a representation, prospectus or circular in respect of any stock of any corporation, and is not transmitted in connection with any sale or offer to sell or by any stock or security now or hereafter to be issued, or with any preliminary negotiation for such sale.